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SUBJECT: PERSPECTIVES ON MINISTER GORDHAN'S MEDIUM TERM
BUDGET POLICY STATEMENT: ECONOMISTS, BUSINESS, LABOR AND
CIVIL SOCIETY GIVE THEIR VIEWS

REF: PRETORIA 02236

¶1. Summary: Representatives from business, labor and civil society gave their views on Finance Minister Gordhan's Medium Term Budget Policy Statement (MTBPS) to the Standing Committee of Finance in Parliament on November 3-4. Most speakers appeared to support the Minister's MTBPS and indicated that he had managed to find the right balance at a very difficult time for the country. Most of them also called for prioritization and greater efficiency in government spending. Sanlam Group Economist Jac Laubscher asserted that the Minister had to manage "a fiscal calamity" and emphasized that greater efficiency and effectiveness in public expenditure was non-negotiable. Business Unity South Africa (BUSA) General Manager Ray Parsons agreed that a budget deficit in the current situation was appropriate, but policy makers would have to make an effort over time to balance it. Federation of South African Unions (FEDUSA) Deputy General Secretary Gretchen Humphries emphasized support for the Minister's focus on expanding employment and strengthening education. The Congress of South African Trade Unions (COSATU) speaker said that while COSATU generally supported Minister Gordhan's budget priorities, it urged government to go beyond job provision to the creation of decent work. End Summary.

¶2. Representatives from business, labor and civil society gave their views on Minister Gordhan's MTBPS to the Parliamentary Standing Committee on Finance during two days of open hearings on November 3-4. Sanlam Group Economist Jac Laubscher and the Institute for Democracy's (IDASA) Len Verwey provided their views on day one. Representatives from Business Unity South Africa (BUSA), the Federation of Unions of South Africa (FEDUSA) and the Congress of South African Trade Unions (COSATU) gave their feedback to the parliamentary committee on day two of the public hearings.

¶3. Laubscher, in his presentation, noted that the public finance situation had deteriorated sharply over the past year with the country having lost fifteen years of progress and having no fiscal space in which to maneuver. He likened Gordhan's MTBPS to the management of a "fiscal calamity." The main thrust of Laubscher's presentation was that the government must prioritize and stream-line public expenditure owing to lower tax revenues resulting from the recession and a growing budget deficit. He pointed out that while tax revenues had declined by 6.2 percent over the past year, expenditure had increased by 17.6 percent during the same time period. Government debt/GDP had also increased to 29.2 percent and would continue to rise over the term of the MTBPS. The increase in debt together with high bond yields would eat up any discretionary public funds in the

government's coffers. Laubscher further lamented the cost of public sector salaries, which he indicated amount to fifty-seven percent of public expenditure. He asserted that this figure should really be less than fifty percent.

¶4. Despite the decline in revenues and the rise in expenditure, Laubscher cautioned against raising taxes. He indicated that South Africa's tax rate at thirty-two percent is already too high for further increases. The average tax rate for middle income countries is around 18.2 percent. If South Africa further increases taxes, it could be a disincentive for investment. Given this tight fiscal position, Laubscher declared that greater efficiency and effectiveness in public expenditure is now non-negotiable.

¶5. IDASA's Len Verwey echoed much of Laubscher's presentation, but he also discussed the divergences occurring between former Minister of Finance Manuel's budget speech in February 2009 and the resulting outcomes later this year. Verwey noted that Manuel had forecast positive economic growth of 1.4 percent for 2009. In reality, there may be a contraction of nearly two percent. Manuel had forecast a budget deficit of 3.8 percent. The deficit is double that figure at 7.6 percent. Moreover, given that economic growth will only increase slowly over the medium term as will tax revenues, the public deficit will remain large and government debt will increase. In a similar manner to Laubscher, Verwey recommended that government focus on eliminating waste and inefficiency in government spending and emphasize job creation.

¶6. BUSA's General Manager Ray Parsons said on day two of the hearings that Minister Gordhan's economic growth forecast of -1.9 percent for 2009 was realistic and in line with BUSA's assessment. He emphasized that government must make a greater effort to ensure that economic growth occurs and that it increases in subsequent years. Parsons also shared BUSA's support for the higher budget deficit of 7.6 percent and indicated that it was appropriate for the country's circumstances. He quickly added, however, that this position must be supported by a "credible path" to a balanced budget. Echoing the economists who went before him, Parsons emphasized the need to "drastically" improve the efficiency of government spending and to "cut its coat according to its cloth." He asserted that failure to do so would delay economic recovery and prolong the government's need to borrow. He also volunteered that the government must strike a careful balance between social investment and investment that will improve competitiveness and generate economic growth. Parsons too warned against the imposition of further taxes to pay for higher public spending. He noted that existing taxes, together with rising input costs, and a relatively small domestic market could discourage increased investment in the country.

¶7. In the expenditure area, Parsons also maintained that there needs to be more discussion on the financing of state-owned enterprises (SOEs), including Eskom. He pointed out that financing SOEs solely from government would significantly increase the overall public sector borrowing requirement which is projected to increase to R285 billion (USD 38 billion). While Parsons supported government investment in needed infrastructure through the SOEs, he urged them to explore and take advantage of public-private partnerships where they could access further funding for expansion programs.

¶8. FEDUSA's Deputy General Secretary Gretchen Humphries expressed support for Minister Gordhan's MTBPS, calling it a well-balanced budget during a very difficult time. Humphries commended the government for effectively using fiscal and monetary policies to mitigate the worst effects of the country's recession and cautioned against withdrawing these policies too early. Humphries' main emphasis was on job creation and skills development. She welcomed the different programs outlined in the Minister's Statement, particularly in regard to the training lay-off schemes and a new phase of the expanded public works program. She also supported the

tax breaks and advisory services to the private sector to further stimulate job creation. Humphries noted, however, that the only solution to the country's unemployment woes and low labor productivity is education and upgrading workers' skills to make them more competitive. Accordingly, Humphries shared that FEDUSA fully supported the Minister's announcement of increased funding to improve the quality of education, student performance and the strengthening of education and training colleges.

¶19. Humphries too emphasized the need to curb government expenditure, especially unnecessary spending on "extravagant luxuries" such as expensive hotel rooms and upgraded airline tickets while traveling on official business. Humphries further pointed out that the R589 million (USD 78.5 million) spent on enlarging the Zuma cabinet could have been used to build more than 10,000 Reconstruction and Development Program (RDP) houses, which would have improved the lives of ordinary South Africans. She regretted that government extravagances and corruption unnecessarily burden the country's tax payers.

¶10. Humphries, on the other hand, shared that her organization was favorably impressed with the Minister's determination to root out corruption in government. She urged it to practice greater transparency and accountability to ensure that the country's future remains secure and not threatened by wasteful programs and expenditures.

¶11. The Congress of South African Trade Unions (COSATU) was the last group to give their presentation to the Standing Committee on Finance. COSATU's Parliamentary Office Coordinator Prakashnee Govender indicated that her organization broadly supports the five spending priorities outlined in the Minister's Statement. She specifically mentioned that COSATU fully supports the extension of the child support grant to the age of eighteen but urged the government to work towards free education. Govender further maintained that the Minister's social security proposals were inadequate and that the government should look at widening the social security nets and incorporating basic income grants. In line with this view, she expressed support for the budget deficit but showed concern over its narrowing in later years.

¶12. Govender further emphasized the overriding need, not just for jobs, but for the creation of decent work with the protection of income security as well as job security. She indicated that the government should focus on procurement from companies who provide decent work and promote local procurement with local content, which would generate more jobs in the country.

¶13. Comment: It is clear that Minister Gordhan has an uphill job in effectively managing South Africa's tight fiscal situation. With declining revenues, an already highly taxed population and a fiscal deficit, his only option for financing programs will be through continued borrowing. Various economists have commented that South Africa could take on additional debt, but they have also urged the Finance Minister to curb government spending. It will have to be tough love for his colleagues in government, who, thus far, do not seem inclined to curb spending. Nevertheless, Gordhan's track record as South African Revenue Service (SARS) Commissioner in eliminating waste and corruption bodes well for his performance as Minister of Finance and for the South African economy. End Comment.